> Covid-19 Client Alert

Federal Reserve Releases Additional Details of the Main Street Lending Program

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On each of June 8, 2020, June 20, 2020, June 26, 2020 and July 15, 2020, the Federal Reserve of Boston (the "Federal Reserve") revised its comprehensive Frequently Asked Questions guide (collectively, the "Updated FAQs") relating to its recently announced Main Street Lending Program (the "Main Street Program"). On June 8, 2020, the Federal Reserve also released revised term sheets for each of the facilities under the Main Street Program (the "Revised Term Sheets"). The Main Street Program is one of a number of federal programs intended to stimulate the economy in the wake of the COVID-19 pandemic. The program includes a Main Street Priority Loan Facility ("MSPLF") in addition to the previously announced Main Street New Loan Facility ("MSNLF") and Main Street Expanded Loan Facility ("MSELF").

This Client Alert updates the information in our April 30, 2020, May 3, 2020, June 2, 2020, and June 28, 2020 Client Alerts regarding the Main Street Program and the Federal Reserve's Frequently Asked Questions. A link to the Federal Reserve's Frequently Asked Questions may be found here, and links to each of the Revised Term Sheets published by the Federal Reserve may be found here: Main Street New Loan Facility, Main Street Expanded Loan Facility, and Main Street Priority Loan Facility.

The Updated FAQs clarify prior guidance published by the Federal Reserve, including by providing further details regarding eligibility criteria, use of proceeds, calculation and payment of interest and fees, and collateral and guarantee requirements, among other things.

What is the Main Street Lending Program?

The Main Street Program is intended to facilitate lending to small and medium-sized US businesses by Eligible Lenders to mitigate the adverse economic impact of the COVID-19 pandemic. Under the program, a special purpose vehicle ("SPV") will purchase up to $600 billion in participations in Eligible Loans, though this size may be adjusted in the future. The Treasury Department, using funds appropriated under the Coronavirus Aid, Relief and Economic Security Act of 2020 (the "CARES Act") will contribute $75 billion in equity to the SPV. Lenders participating in the Main Street Program will either provide new loans to Borrowers or increase ("upsize") existing term loans. The SPV will purchase participations in the loans funded under the

Main Street Program. Lenders eligible to participate in the program are U.S. insured depositary institutions, U.S. bank holding companies, U.S. savings and loan holding companies, and U.S. branches, agencies and intermediate holding companies of foreign banks or any of their subsidiaries.

What are the Borrower eligibility requirements under the Main Street Program?

Loans under the Main Street Program will be provided by Eligible Lenders to businesses with up to 15,000 employees or with revenues of less than $5 billion for 2019.[1] Eligible Borrowers include corporations, partnerships, limited liability companies, associations, trusts, joint ventures with no more than 49% participation by non-US business entities, and tribal business concerns[2]. While non-profit organizations are not eligible, the Federal Reserve announced in the Updated FAQs that it is planning to establish one or more loan programs suitable for non-profit organizations soon. Sole proprietorships are not eligible.

In order to determine whether a Borrower meets the size standards, the Borrower must take into account employees and revenues of its affiliates. Both employee count and affiliation are determined under pre-existing rules established by the Small Business Administration (the "SBA"). "Employees" include full-time, part-time, seasonal or otherwise employed persons, but exclude volunteers and independent contractors, and are calculated based on the average for each pay period during the 12 months prior to origination or upsizing of a Main Street Program loan. "Revenue" may be calculated based on "revenue", per GAAP-based audited financial statements, or based upon annual "receipts" reported to the Internal Revenue Service, per existing SBA rules. Borrowers may choose which revenue calculation methodology to use. If audited financial statements or receipts are not yet available, the most recent audited financial statements or receipts should be used.

Borrowers under the Main Street Program must have been established prior to March 13, 2020 in the United States (including its territories and possessions) or be an Indian Tribal government. A Borrower may be a subsidiary of a foreign company so long as the Borrower itself was created or organized in the United States or under the laws of the United States and meets the US significant operations requirements. However, the use of the proceeds of a Main Street loan may not be used for the benefit of a Borrower's foreign parents, affiliates or subsidiaries.

Borrowers are required to have significant operations and a majority of their employees, in the United States. The Updated FAQs clarified that the evaluation of whether a Borrower has "significant operations" in the United States should be based on the consolidated operations of the Borrower and its subsidiaries and exclude the operations of the Borrower's parents and sister companies. The Updated FAQs included a list of examples of when Borrowers (together with their subsidiaries) will be deemed to have significant operations in the United States.[3]

In order to be eligible for the MSELF, the existing credit facility must have originated before April 24, 2020 and must have a remaining maturity of at least 18 months.[4]

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[1] These thresholds represent increases from the 10,000 and $2.5 billion, respectively, announced in previous Federal Reserve guidance. The size criteria under the Main Street Program are notable because the assistance for mid-size businesses under the Coronavirus Economic Stabilization Act ("CESA") enacted as part of the CARES Act restricts eligibility to borrowers with between 500 and 10,000 employees, leaving many small and mid-sized businesses with fewer than 500 employees ineligible for programs supported by the Treasury Department and the Federal Reserve. The Main Street Program appears to close this gap.

[2] On July 15, 2020, the Updated FAQs clarified that a tribal business concern must be a separate and distinct legal entity organized or chartered by the tribe, Federal, or state authorities, and that the lender must determine, based on its own due diligence and advice from counsel, that a tribal business either does not have or has effectively waived sovereign immunity such that matters resulting from the Main Street Loan Program may be brought in US Federal courts or state courts as courts of competent jurisdiction.

[3] The non-exhaustive list of examples included Borrowers that, together with their subsidiaries have, greater than 50% of (i) their assets located in the United States; (ii) annual net income generated in the United States; (iii) annual net operating revenues generated in the United States; or (iv) annual consolidated operating expenses (excluding interest expense and any other expenses associated with debt services) generated in the United States.

[4] A lender is allowed to amend the existing credit facility to provide for a maturity of at least 18 months in order to qualify for a loan for the MSELF program.

Borrowers must have been in good financial standing before the COVID-19 crisis and require financing as a result of exigent circumstances arising out of the COVID-19 pandemic. Any pre-existing debt of a Borrower with a lender under the Main Street Program must have an internal risk rating equivalent to "pass" in the Federal Financial Institutions Examination Council's supervisory rating system, as of December 31, 2019 (or at the time of origination if the existing loan was originated after December 31, 2019).

Entities directly or indirectly controlled by the President or Vice President of the United States, members of Congress, the head of any Executive department or any of their spouses, children, sons-in-law or daughters-in-law are ineligible. The individuals are considered to control an entity if they own, control or hold twenty percent or more (by vote or value) of any class of equity ownership interest in the entity.

Certain businesses which are ineligible for SBA loans are also ineligible under the Main Street Program. These include financial businesses primarily engaged in the business of lending, passive businesses owned by developers and landlords that do not actively use or occupy the assets acquired or developed with loan proceeds, life insurance companies, business located in a foreign country, pyramid sale distribution plans, businesses deriving more than one-third gross annual revenue from gambling, government-owned entities, businesses engaged in illegal activity, private clubs, certain loan packagers, businesses with certain related parties have been incarcerated or indicted for a felony or crime of moral turpitude, businesses in which the lender or its related parties own equity and businesses which present live performances of a prurient sexual nature or derive revenue from the sale of products or services or display of activities of a prurient sexual nature. Each Borrower is expected to review the list of ineligible businesses in 13 CFR 120.110(b)-(i) and (m) – (s) and make a reasonable good-faith effort to determine if it is classified within one of the listed ineligible categories.

Are there specific eligibility requirements for private equity funds and their portfolio companies or other entities that may be deemed "affiliated"?

The Updated FAQs clarify that, contrary to earlier guidance, private equity funds are ***not*** eligible for Main Street Program loans. However, private equity-owned portfolio companies that meet employee and revenue requirements (together with their affiliates, as determined in 13 CFR 121.301(f)) may apply for Main Street Program loans if they meet all other eligibility requirements.

In addition, the Updated FAQs state that affiliated entities may only participate in a single facility and the borrowings of all affiliated entities count toward the applicable borrowing limits. "Facility" in this context appears to mean one of the MSNLF, MSELF and MSPLF. The Updated FAQs do not expressly state, but seem to suggest, that these limitations apply to affiliated portfolio companies of private equity funds. Further guidance on this point is needed to clarify the Federal Reserve's intent regarding this matter.[5]

What are the terms of loans made under the Main Street Program?

The MSNLF, MSPLF and MSELF all share certain common terms and differ in certain key aspects. A summary of the principal similarities and differences follows. For a chart comparing the facilities, please click here.

What are the terms of loans made under the Main Street Program?

All three facilities have many of the same features, including the following:

- Maturity: 5 years.[6]

[5] The Updated FAQs clarified that if only one business from an affiliated group is seeking funding through a Main Street program, the affiliated group's debt and EBITDA are not applicable to the determination of the business's debt and EBITDA for purposes of qualification or loan size (except to the extent that the borrower's subsidiaries' financials are consolidated with the borrower's). However, if the business seeking funding has an affiliate that has already sought funding from a Main Street facility, then the entire affiliate group's debt and EBITDA are relevant to such determination.

[6] Under previous Federal Reserve guidance, maturity was 4 years.

- Interest: Adjustable rate interest at LIBOR +300, payable consistent with a lender's other similarly situated loans after the first year of deferral.[7]
- Amortization and Payment: Payments of principal are deferred for two years and payments of interest are deferred for one year (interest is capitalized). After the second year, loans are amortized over the remaining three-year term.[8]
- Prepayment Penalty: None.
- Repayment: 15% of the principal amount (including capitalized interest) is due at the end of each of years three and four, with the remaining 70% due at maturity.[9]
- Restrictions on Use of Proceeds: Program loans may not be used for:
  - the benefit of an Eligible Borrower's foreign parents, affiliates, or subsidiaries (use by domestic affiliates is permissible); or
  - to refinance or accelerate payment of existing debt, except (i) at the time of origination of an MSPLF Loan if the debt was owed to a different, unaffiliated lender, or (ii) under the limited exception for mandatory and due debt and interest payments after the original of the Main Street loan.

However, the facilities differ in certain key aspects, including the following:

- New/Upsize Loans: Under MSNLF and MSPLF, lenders extend new loans to Borrowers. Under MSELF, lenders "upsize", or increase, existing credit facilities.
- Loan Size: Under MSNLF loan size ranges from $250,000 to $35 million. Under MSPLF, loan size ranges from $250,000 to $50 million.[10] Under MSELF, the upsized tranche ranges from $10 million to $300 million.[11] Borrowers may not borrow less than the applicable minimum. Loans under MSNLF, together with existing outstanding and undrawn debt, cannot exceed four times 2019 EBITDA. Loans under MSPLF, together with existing outstanding and undrawn debt, cannot exceed six times 2019 adjusted EBITDA. Loans under MSELF cannot exceed six times 2019 adjusted EBITDA when added to existing outstanding and available undrawn debt. The Updated FAQs provide guidance on calculation of existing indebtedness and EBITDA, including adjustments.
- Priority and Security: All loans under the Main Street Program must be senior or *pari passu* in terms of priority to the Borrower's other loans and debt instruments (other than, in the case of MSELF and MSPLF loans, mortgage debts[12]). However, MSPLF and MSELF must be secured if, at the time of origination, the Borrower has any other secured loans or debt instruments, other than mortgage debt. However, a MSPLF loan need not share in all of the collateral that secures the Borrower's other loans or debt instruments. In addition, the Updated FAQs provide details on the specific collateral coverage ratio that any secured MSPLF loan must meet at the time of origination. Any collateral securing the MSELF loans must secure the underlying loan and the upsized tranche on a pro rata basis. Further, a lender may not

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[7] Under previous Federal Reserve guidance, interest was based on SOFR. Also, on July 15, 2020, the Federal Reserve updated guidance to clarify that LIBOR floors are not permissible.

[8] Under previous Federal Reserve guidance, principal payments were deferred for one year.

[9] Under previous Federal Reserve guidance, one-third of the principal amount (including capitalized interest) of MSNLF loans was due at the end of each of years two and three, with the remaining one-third due at maturity and 15% of the principal amount (including capitalized interest) of MSPLF and MSELF was due at the end of each of years two and three, with the remaining 70% due at maturity.

[10] Under previous Federal Reserve guidance, minimum loan size for each of MSNLF and MSPLF was $500,000 and the maximum loan size was $25 million.

[11] Under previous Federal Reserve guidance, maximum upsized tranche loan size for MSELF was $200 million.

[12] In the July 15, 2020 Updated FAQs, the definition of "mortgage debt" was clarified to reflect that debt secured by real property qualifies as mortgage debt only if it is solely secured by real property. MSPLF loans extended in good faith on or before July 17, 2020 that do not reflect this clarification are not adversely affected by the clarification.

require a borrower to provide collateral or guarantees solely with respect to the lender's 5% retained portion of the Main Street Program loan. Any collateral pledged or guarantees made in connection with a Main Street Program loan must apply to the entirety of a MSNLF loan, MSPLF loan, or the upsized tranche of a MSELF loan.

- Restrictions on Indebtedness: At the time of origination, loans under MSPLF may be used to refinance existing debt held by a lender that is not eligible to participate in the Main Street Program (i.e., the proceeds of a MSPLF may be used to refinance existing loans owed to lenders other than the lender of the MSPLF loan) and is not an affiliate of the MSPLF lender. Otherwise, Borrowers may not prepay any principal on existing indebtedness, or cancel or reduce any existing credit lines. Borrowers are permitted to make regularly scheduled debt payments, repay lines of credit in accordance with their terms, obtain new indebtedness in the ordinary course of business that is secured by newly-acquired property and is not senior to the Main Street Program loan, and refinance debt that is maturing no later than 90 days from the date of such refinancing.
- Fees: Lenders may choose, but are not required to, charge a fee of 100 basis points on MSNLF and MSPLF loans and 75 bps on MSELF loans.[13] Additional transaction fees may be charged but must be passed on the SPV. No other fees, except *de minimis* fees for services that are customary and necessary, may be charged. Lenders may charge customary consent fees if such fees are necessary to amend loan documentation in connection with upsizing a loan through MSELF. Fees may be included in the principal amount of the loans so long as their inclusion does not cause the total loan size to exceed the maximum amount permitted under the applicable Main Street Program.

While loan size is currently being determined based upon EBITDA, the Federal Reserve and the Treasury Department are evaluating the feasibility of adjusting metrics to account for asset-based criteria.

Are loans under the Main Street Program forgivable?

No. Loans extended under each of the Main Street Programs are not subject to forgiveness. In the event of restructurings or workouts, the SPV may agree to a reduction in interest (including capitalized interest), extended amortization schedules and maturities, and higher priority "priming" loans.

If a Borrower is able to receive credit from other sources is it still eligible for a Main Street loan?

A Borrower must demonstrate that it is unable to secure adequate credit accommodations from other credit sources available to the Borrower. "Lack of adequate credit accommodations" does not mean that no credit from other sources is available to the Borrower, but rather that the amount, price or terms of the credit available from other sources is inadequate for the Borrower's needs during the current unusual and exigent circumstances. Borrowers are required to certify as to this inadequacy but do not need to show that applications for credit have been denied by other lenders or provide documentation that the amount, price or terms of credit available elsewhere is inadequate.

What covenants and certifications must Borrowers make?

The Updated FAQs provide details around covenants and certification requirements for Borrowers. Required covenants include provisions regarding (i) priority and/or security of the loan, (ii) a mandatory prepayment requirement for material breaches of the Borrower's certification, including any material misrepresentation, (iii) cross-acceleration and cross-defaults, and (iv) financial reporting.

Borrowers are required to make certain certifications including certifications regarding the date of business establishment, number of employees and revenues, lack of participation in other Main Street Programs and the Primary Market Corporate Credit Facility, jurisdiction of organization and operation, lack of conflicts of interest,

[13] Under previous Federal Reserve guidance, a fee of 100 bps applied to all loans.

and a commitment to comply with compensation and stock repurchase restrictions. Borrowers also must certify that they have a reasonable basis to believe that, after giving effect to the loan, they have the ability to meet their financial obligations and do not expect to file for bankruptcy for at least 90 days. Borrowers must also certify that they will comply with the following during the term of the Main Street Program loan and for the 12-month period after the loan has been repaid:

- Borrowers and their parent entities may not repurchase any equity security listed on a national securities exchange (other than as required pursuant to contracts in place prior to March 27, 2020).
- Borrowers may not pay dividends or make other distributions with respect to common stock, except in the case of tax distributions by pass-through entities.
- Borrowers may not provide "total compensation" (as discussed below) during any consecutive 12-month period which exceeds 2019 total compensation to any employees or officers whose total compensation exceeded $425,000 in 2019.
- Borrowers may not provide severance or other termination benefits in excess of two times 2019 total compensation to any employees or officers whose total compensation exceeded $425,000 in 2019.
- Borrowers may not provide total compensation during any consecutive 12-month period which exceeds the sum of (a) $3 million, plus (b) 50% of 2019 total compensation in excess of $3 million to any employees or officers whose total compensation exceeded $3 million in 2019.

How is Total Compensation Defined?

Total Compensation is broadly defined and includes salary, bonuses, awards of stock and other eligible benefits, but does not include the value of severance pay or other benefits paid to an employee in connection with the termination of employment.

How is Total Compensation Calculated?

Public company borrowers must calculate Total Compensation using the methodology described in Item 402(c) of the Securities and Exchange Commission's Regulation S-K. For these borrowers, this essentially means that they would use the "accrual method" to determine Total Compensation.

Private company borrowers who have gross revenues equal to or less than $10 million for 2019 may elect to calculate Total Compensation using federal tax rules (essential the "cash method") or under the SEC's method. However, even those private company borrowers who have gross revenues greater than $10 million can elect to use the federal tax method for those employees whose Total Compensation is $425,000 or less, or who defer less than 30% of their Total Compensation.

The election must be made when the Main Street loan is disbursed and the method elected must be used for so long as the loan is outstanding, plus 12 months (unless required to switch; see below).

When Can a Company be required to switch from the Federal Tax Method to the SEC Method?

If a private company borrower goes public, it will be required to switch to the SEC method. In addition, a switch to the SEC method is mandated for employees whose Total Compensation increases to $425,000 or more, and defer 30% or more of their Total Compensation.

The complete instructions and guidance on the Borrower Certification and Covenants released by the Federal Reserve are available for MSNLF, MSPLF, and MSELF.

What is the application process?

To obtain a loan under the Main Street Program, a Borrower must submit an application to an Eligible Lender. In addition to the minimum loan requirements laid out under the program, lenders are expected to assess each Borrower's financial condition at the time of application and apply their own underwriting standards. Borrowers that meet the eligibility criteria may not receive the maximum allowable loan, or be approved for a loan in the first instance.

During what periods will the Main Street Program be in effect?

The official launch date of the Main Street Program and the time and date at which the SPV will begin purchasing participations has not yet been announced. Current guidance indicates that the SPV will purchase loans until September 30, 2020, unless the Main Street Program is extended by the Federal Reserve and the Treasury Department.

May borrowers and their affiliates take advantage of multiple stimulus programs?

The Federal Reserve has expressly stated that Borrowers that have obtained Paycheck Protection Loans or Economic Injury Disaster Loans may also obtain loans under the Main Street Program. Paycheck Protection Loans that have not been forgiven will be counted as outstanding debt for the purposes of the Main Street Program's maximum loan size test. However, Borrowers may not receive a new loan and upsize an existing loan under the Main Street Program. Borrowers under the Main Street Program may not participate in the Primary Market Corporate Credit Facility or the $17 billion allocated under CESA to benefit businesses deemed critical to national security.

How will the SPV participate in the loans made under the Main Street Program?

The SPV will purchase, at par value, a 95% participation in each MSNLF loan, MSPLF loan, and MSELF new loan tranche.[14] For loans under MSNLF and MSPLF, each lender must retain the balance until (i) the loan matures or (ii) either the SPV or a governmental assignee sells all of its participation in the loan, whichever comes first. For loans under the MSPLF, each lender must retain the balance until the loan matures, the upsized tranche matures, or the SPV sells all of its participation, whichever comes first. Losses would be shared between the SPV and the lender on a *pari passu* basis.

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Morrison Cohen LLP has created the COVID-19 Resource Taskforce, a multidisciplinary taskforce comprised of attorneys with deep expertise in a broad range of legal areas, to assist clients navigating the challenging and uncertain business and legal environment caused by the COVID-19 pandemic. We encourage clients to utilize our capabilities by reaching out to their primary Morrison Cohen attorney contact, who will put you in touch with the appropriate Taskforce person. You may also reach out directly to Joe Moldovan and Alec Nealon, the Taskforce co-chairs:

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[14] Under previous Federal Reserve Guidance, the SPV was only to purchase an 85% participation in each MSPLF loan.

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